



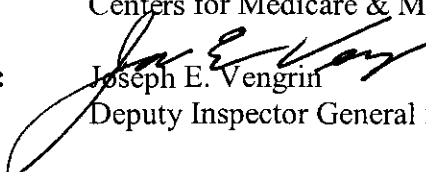
DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Washington, D.C. 20201

FEB - 4 2005

**TO:** Tim Hill  
Director, Office of Financial Management  
Centers for Medicare & Medicaid Services

**FROM:**  Joseph E. Vengrin  
Deputy Inspector General for Audit Services

**SUBJECT:** Review of Blue Cross Blue Shield of Florida's Pension Segmentation  
Requirements for the Period January 1, 1994, to January 1, 2003 (A-07-04-00172)

Attached is an advance copy of our final report on Blue Cross Blue Shield of Florida's (Florida) pension segmentation requirements. We will issue this report to Florida within 5 business days. We suggest that you share this report with the Centers for Medicare & Medicaid Services components involved with monitoring the Medicare contractors' financial operations, particularly the Center for Medicare Management and the Office of the Actuary.

Florida is a Medicare contractor and, as such, is allowed to claim reimbursement for its Medicare employees' pension costs. Regulations and the Medicare contracts provide for pension segmentation requirements and the update of segment assets. We are recommending that Florida increase Medicare segment assets by about \$1.3 million. Florida agreed with our report findings.

If you have any questions or comments about this report, please do not hesitate to call me, or George M. Reeb, Assistant Inspector General for the Centers for Medicare & Medicaid Audits, at (410) 786-7104 or James P. Aasmundstad, Regional Inspector General, Region VII, at (816) 426-3591, extension 225. Please refer to report number A-07-04-00172 in all correspondence.

Attachment



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General  
Offices of Audit Services

Report Number: A-07-04-00172

FEB - 8 2005

Region VII  
801 East 12th Street  
Room 284A  
Kansas City, Missouri 64106

Ms. Sandy L. Coston  
President & Chief Operating Officer  
First Coast Service Options, Inc.  
532 Riverside Avenue 20T  
Jacksonville, Florida 32202

Dear Ms. Coston:

Enclosed are two copies of the Department of Health and Human Services (HHS), Office of Inspector General (OIG) report entitled "Review of Blue Cross Blue Shield of Florida's Pension Segmentation Requirements for the Period January 1, 1994, to January 1, 2003." A copy of this report will be forwarded to the action official noted below for review and any action deemed necessary.

The HHS action official named below will make final determination as to actions taken on all matters reported. We request that you respond to the HHS action official within 30 days. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

In accordance with the principles of the Freedom of Information Act (5 U.S.C. § 552, as amended by Public Law 104-231), OIG reports issued to the Department's grantees and contractors are made available to members of the press and general public to the extent the information is not subject to exemptions in the Act that the Department chooses to exercise (see 45 CFR part 5).

Please refer to report number A-07-04-00172 in all correspondence.

Sincerely yours,

James P. Aasmundstad  
Regional Inspector General  
for Audit Services

Enclosure - as stated

**Direct Reply to HHS Action Official:**

Ms. Rose Crum-Johnson  
Regional Administrator  
Centers for Medicare & Medicaid Services  
Department of Health and Human Services  
61 Forsyth Street, S.W., Suite 4T20  
Atlanta, Georgia 30303-8909

**Department of Health and Human Services**

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF BLUE CROSS  
BLUE SHIELD OF FLORIDA'S  
PENSION SEGMENTATION  
REQUIREMENTS FOR THE  
PERIOD JANUARY 1, 1994, TO  
JANUARY 1, 2003**



**FEBRUARY 2005  
A-07-04-00172**

# ***Office of Inspector General***

**<http://oig.hhs.gov>**

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In accordance with the principles of the Freedom of Information Act (5 U.S.C. 552, as amended by Public Law 104-231), Office of Inspector General, Office of Audit Services reports are made available to members of the public to the extent the information is not subject to exemptions in the act. (See 45 CFR part 5.)

## **OAS FINDINGS AND OPINIONS**

The designation of financial or management practices as questionable or a recommendation for the disallowance of costs incurred or claimed, as well as other conclusions and recommendations in this report, represent the findings and opinions of the HHS/OIG/OAS. Authorized officials of the HHS divisions will make final determination on these matters.



## **EXECUTIVE SUMMARY**

### **BACKGROUND**

Blue Cross Blue Shield of Florida (Florida) administers Medicare Parts A and B operations under a cost reimbursement contract with the Centers for Medicare & Medicaid Services (CMS).

Starting with fiscal year (FY) 1988, CMS incorporated segmentation requirements into Medicare contracts. The Medicare contract defines a segment and specifies the methodology for the identification and initial allocation of pension assets to the segment. Additionally, the contract requires Medicare segment assets to be updated for each year after the initial allocation in accordance with Cost Accounting Standards (CAS) 412 and 413.

We previously conducted a segmentation review (A-07-94-01107) that addressed the update of the segment's assets from January 1, 1990, to January 1, 1994.

### **OBJECTIVES**

The objectives of our review were to determine if Florida:

- implemented our prior audit recommendation and
- complied with the Medicare contract's pension segmentation requirements while updating Medicare segment assets from January 1, 1994, to January 1, 2003.

### **SUMMARY OF FINDINGS**

Florida did not implement the prior audit recommendation to increase Medicare segment assets by \$813,122 and did not comply with the Medicare contract's pension segmentation requirements while updating Medicare segment assets from January 1, 1994, to January 1, 2003. Florida understated Medicare segment assets by \$1,294,606. Florida did not ensure that our prior audit recommendation was implemented and that segment assets were updated in accordance with the Medicare contract.

### **RECOMMENDATIONS**

We recommend that Florida:

- increase the Medicare segment pension assets by \$1,294,606 as of January 1, 2003,
- implement controls to ensure that audit recommendations are addressed, and
- implement controls to ensure that Medicare segment assets are updated in accordance with the Medicare contract.

## **AUDITEE’S COMMENTS**

Florida agreed with our report findings. Florida’s comments are presented in Appendix B to this report.

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## **Glossary of Abbreviations and Acronyms**

CAS	Cost Accounting Standards
CMS	Centers for Medicare & Medicaid Services
FY	fiscal year
FAR	Federal Acquisition Regulations
OIG	Office of Inspector General
WAV	weighted average value

## **INTRODUCTION**

### **BACKGROUND**

#### **Florida's Medicare Contract**

Florida administers Medicare Parts A and B operations under a cost reimbursement contract with CMS. In claiming costs, contractors must follow cost reimbursement principles contained in the Federal Acquisition Regulations, CAS, and the Medicare contract.

CMS incorporated segmentation requirements into Medicare contracts starting in FY 1988. The Medicare contract defines a segment and specifies the methodology for the identification and initial allocation of pension assets to the segment. Furthermore, the contract requires Medicare segment assets to be updated for each year after the initial allocation in accordance with CAS 412 and 413.

Our previous segmentation review (A-07-94-01107) addressed the update of the segment's assets from January 1, 1990, to January 1, 1994.

#### **Regulations**

CAS 412 regulates the determination and measurement of pension cost components. It also regulates the assignment of pension costs to appropriate accounting periods.

CAS 413 regulates the valuation of pension assets, allocation of pension costs to segments of an organization, adjustment of pension costs for actuarial gains and losses, and assignment of gains and losses to cost accounting periods.

### **OBJECTIVES, SCOPE, AND METHODOLOGY**

#### **Objectives**

The objectives of our review were to determine if Florida:

- implemented our prior audit recommendation and
- complied with the Medicare contract's pension segmentation requirements while updating Medicare segment assets from January 1, 1994, to January 1, 2003.

#### **Scope**

We reviewed Florida's identification of the Medicare segment and its update of Medicare assets from January 1, 1994, to January 1, 2003. Achieving our objectives did not require that we review Florida's overall internal control structure. However, we did review controls relating to the identification of the Medicare segment and the update of the segment assets to ensure adherence to the Medicare contract, CAS 412, and CAS 413.

We performed onsite audit work at Florida's office in Jacksonville, FL during June of 2004.

## Methodology

In performing this review, we used information provided by Florida's actuarial consulting firms. The information included assets, liabilities, normal costs, contributions, benefit payments, investment earnings, and administrative expenses. We reviewed Florida's accounting records, pension plan documents, annual actuarial valuation reports, and Department of Labor/Internal Revenue Service Form 5500s. The CMS Office of the Actuary staff used the documents to calculate Medicare segment assets as of January 1, 2003. We reviewed the methodology and calculations.

We performed this review in conjunction with our audits of unfunded pension costs (A-07-04-00179) and pension costs claimed for Medicare reimbursement (A-07-04-00180). We used the information obtained and reviewed during those audits in performing this review.

Appendix A to this report presents details for the updated pension assets of the Medicare segment from January 1, 1994, to January 1, 2003.

We performed our review in accordance with generally accepted government auditing standards.

## FINDINGS AND RECOMMENDATIONS

Florida did not implement the recommendation from the prior audit. Florida did not ensure that our prior audit recommendation was implemented and that Medicare segment assets were updated in accordance with the Medicare contract. As a result, as of January 1, 2003, Florida understated Medicare segment pension assets by \$1,294,606.

### Summary of Asset Adjustments

Prior Audit Recommendation	\$813,122
Contributions	(488,944)
Benefit Payments	273,419
Transfers	(658,701)
Earnings and Expenses	1,355,710
(Over)/UnderStatement	<u><u>\$1,294,606</u></u>

## MEDICARE CONTRACT AND CAS REQUIREMENTS

### Medicare Contract

The Medicare contract identifies a Medicare segment as:

“ . . . any organizational component of the contractor, such as a division, department, or other similar subdivision, having a significant degree of responsibility and accountability for the Medicare contract/agreement, in which:

1. The majority of the salary dollars is allocated to the Medicare agreement/contract; or,
2. Less than a majority of the salary dollars is allocated to the Medicare agreement/contract, and these salary dollars represent 40 percent or more of the total salary dollars allocated to the Medicare agreement/contract.”

Furthermore, the Medicare contract states that “. . . the pension assets allocated to each Medicare segment shall be adjusted in accordance with the CAS 413.50(c)(7).”

### **Cost Accounting Standards**

The CAS 413.50(c)(7) requires that the asset base be adjusted by contributions, permitted unfunded accruals, income, benefit payments, and expenses. In addition, CAS 413.50(c)(8) requires an adjustment for transfers (participants who enter or leave the segment) if the transfers materially affect the segment’s ratio of pension plan assets to actuarial accrued liabilities.

According to CAS 412.50(a)(4), prepayment credits are funds available to the contractors at the beginning of plan years. Funds should be applied first to satisfy funding requirements in order to reduce interest costs to the Government.

### **COMPONENTS OF ASSET UPDATE**

#### **Prior Audit Recommendation**

Florida did not implement the recommendation from our prior audit report. Our previous segmentation report (A-07-94-01107) addressed the update of the Medicare segment’s assets from January 1, 1990, to January 1, 1994. In that report, we recommended that Florida increase segment assets from \$17,338,906 to \$18,152,028 (an increase of \$813,122) as of January 1, 1994.

#### **Contributions and Prepayment Transfers Overstated**

Florida’s update methodology did not equitably assign pension contributions to the Medicare segment because the Medicare asset value adjustment from the prior audit had not been implemented. In addition, Florida incorrectly identified the 2002 Medicare segment. As a result, Florida overstated segment assets by \$488,944.

For years 1994 through 2002, Florida’s contributions exceeded the required funding of the CAS pension costs. According to CAS, amounts funded in excess of pension costs (or prepayments) shall be carried forward with interest to fund future CAS pension costs. Our computations considered the excess contributions and made prepayment adjustments to fund CAS pension costs of the Medicare segment.

The audited update of Medicare segment assets assigned contributions to the Medicare segment using the pension costs as calculated by the CMS Office of the Actuary. The segment assets decreased by \$488,944 in the audited update due to differences in assigned contributions. A comparison of the Office of Inspector General’s (OIG) and Florida’s calculations of pension contributions and prepayment transfers follows.

<b>Contributions and Prepayment Transfers</b>			
<b>Year</b>	<b>OIG</b>	<b>Florida</b>	<b>Difference</b>
1994	\$1,788,675	\$1,654,796	\$133,879
1995	1,379,432	1,359,360	20,072
1996	2,383,750	2,437,733	(53,983)
1997	2,288,828	2,288,773	55
1998	2,050,531	1,960,346	90,185
1999	2,212,895	2,078,572	134,323
2000	0	0	0
2001	2,571,048	2,583,992	(12,944)
2002	3,055,456	3,855,987	(800,531)
<b>TOTAL</b>	<b>\$17,730,615</b>	<b>\$18,219,559</b>	<b>(\$488,944)</b>

### **Benefit Payments Overstated**

Florida's update of segment assets did not properly identify benefit payments to retirees from the Medicare segment. Using Florida's methodology, we identified the actual benefits paid to the retirees from the segment and assigned the costs to the segment. As a result, Florida overstated segment benefit payments and understated segment assets by \$273,419.

### **Transfers Overstated**

Florida made adjustments for transfers in its update of Medicare segment assets from January 1, 1994, to January 1, 2003. However, Florida incorrectly identified the participants who transferred in and out of the segment, which resulted in an overstatement of assets of \$658,701. Transfers for the audited update were adjusted based on our revisions to the Medicare segment.

A comparison of OIG's and Florida's calculations of net asset transfers from the segment is shown below.

<b>Net Asset Transfers From the Medicare Segment</b>			
<b>Year</b>	<b>OIG</b>	<b>Florida</b>	<b>Difference</b>
1994	(\$101,168)	\$146,844	(\$248,012)
1995	(982,732)	(377,488)	(605,244)
1996	(688,707)	(1,483,736)	795,029
1997	(950,714)	(247,589)	(703,125)
1998	(392,778)	(158,417)	(234,361)
1999	(311,159)	(230,686)	(80,473)
2000	(85,135)	(1,968)	(83,167)
2001	(2,349,139)	(230,787)	(2,118,352)
2002	(2,278,291)	(4,897,295)	2,619,004
<b>TOTAL</b>	<b>(\$8,139,823)</b>	<b>(\$7,481,122)</b>	<b>(\$658,701)</b>

### **Earnings and Expenses Understated**

Florida understated its investment earnings, less administrative expenses, by \$1,355,710 because it did not adjust the Medicare segment's asset value as recommended in the prior audit. In addition, the Medicare asset base was developed using incorrect contribution, transfer, and benefit amounts (discussed above). It was Florida's practice to allocate investment income to the segment based on beginning-of-the-year asset values. Administrative expenses to the segment were allocated in proportion to the allocation of earnings. However, for plan years beginning after March 30, 1995, CAS required investment income and expenses to be allocated among segments based on the ratio of the segment's weighted average value (WAV) of assets to total company WAV of assets. The audited update of Medicare segment assets reflects the required change in methodology.

### **UNDERSTATEMENT OF MEDICARE SEGMENT ASSETS**

Florida did not ensure that our prior audit recommendation was implemented. In addition, Florida did not ensure that Medicare segment pension assets were updated in accordance with the Medicare contract. As a result, as of January 1, 2003, Florida understated Medicare segment pension assets by \$1,294,606.

### **RECOMMENDATIONS**

We recommend that Florida:

- increase the Medicare segment pension assets by \$1,294,606 as of January 1, 2003,
- implement controls to ensure that audit recommendations are addressed, and
- implement controls to ensure that Medicare segment assets are updated in accordance with the Medicare contract.

## **AUDITEE'S COMMENTS**

Florida agreed with our report findings. Florida's comments are presented in Appendix B to this report.

# **APPENDIXES**



**BLUE CROSS BLUE SHIELD OF FLORIDA**  
**STATEMENT OF MEDICARE PENSION ASSETS FOR**  
**1994 TO 2003**

Description		Total Company	Other Segment	Medicare
Assets January 1, 1994	<u>1/</u>	\$98,730,170	\$80,578,142	\$18,152,028
Prepayment Transfer		0	0	0
Contributions	<u>2/</u>	12,484,472	10,695,797	1,788,675
Earnings	<u>3/</u>	567,974	463,549	104,425
Benefit Payments	<u>4/</u>	(4,962,396)	(4,710,639)	(251,757)
Expenses	<u>5/</u>	(494,001)	(403,176)	(90,825)
Transfers	<u>6/</u>	0	101,168	(101,168)
Assets January 1, 1995		106,326,219	86,724,841	19,601,378
Prepayment Transfer	<u>7/</u>	0	(513,090)	513,090
Contribution		12,935,979	12,069,637	866,342
Earnings		28,411,453	23,036,661	5,374,792
Benefit Payments		(2,402,868)	(2,345,157)	(57,711)
Expenses		(509,267)	(412,925)	(96,342)
Transfers		0	982,732	(982,732)
Assets January 1, 1996		144,761,516	119,542,699	25,218,817
Prepayment Transfer		0	(1,454,573)	1,454,573
Contribution		13,579,701	12,650,524	929,177
Earnings		22,031,026	17,969,389	4,061,637
Benefit Payments		(5,548,165)	(4,554,952)	(993,213)
Expenses		(689,156)	(562,103)	(127,053)
Transfers		0	688,707	(688,707)
Assets January 1, 1997		174,134,922	144,279,691	29,855,231
Prepayment Transfer		0	(1,492,947)	1,492,947
Contribution		13,555,415	12,759,534	795,881
Earnings		33,888,187	27,727,685	6,160,502
Benefit Payments		(5,884,013)	(5,429,661)	(454,352)
Expenses		(871,678)	(713,216)	(158,462)
Transfers		0	950,714	(950,714)
Assets January 1, 1998		214,822,833	178,081,800	36,741,033

**BLUE CROSS BLUE SHIELD OF FLORIDA**  
**STATEMENT OF MEDICARE PENSION ASSETS FOR**  
**1994 TO 2003**

Description	Total Company	Other Segment	Medicare
Assets January 1, 1998	214,822,833	178,081,800	36,741,033
Prepayment Transfer	0	(1,401,593)	1,401,593
Contribution	13,840,673	13,191,735	648,938
Earnings	34,031,737	27,968,973	6,062,764
Benefit Payments	(7,592,515)	(6,496,157)	(1,096,358)
Expenses	(1,026,877)	(843,939)	(182,938)
Transfers	0	392,778	(392,778)
Assets January 1, 1999	254,075,851	210,893,597	43,182,254
Prepayment Transfer	0	(1,424,759)	1,424,759
Contribution	13,157,274	12,369,138	788,136
Earnings	41,273,745	33,958,953	7,314,792
Benefit Payments	(8,478,079)	(7,819,346)	(658,733)
Expenses	(1,066,849)	(877,775)	(189,074)
Transfers	0	311,159	(311,159)
Assets January 1, 2000	\$298,961,942	\$247,410,967	\$51,550,975
Prepayment Transfer	0	0	0
Contribution	18,160,845	18,160,845	0
Earnings	(12,750,153)	(10,541,152)	(2,209,001)
Benefit Payments	(9,544,748)	(8,381,211)	(1,163,537)
Expenses	(2,702,705)	(2,234,454)	(468,251)
Transfers	0	85,135	(85,135)
Assets January 1, 2001	\$292,125,181	\$244,500,130	\$47,625,051
Prepayment Transfer	0	(1,912,210)	1,912,210
Contribution	27,481,529	26,822,691	658,838
Earnings	(14,151,949)	(11,746,477)	(2,405,472)
Benefit Payments	(13,077,278)	(11,087,665)	(1,989,613)
Expenses	(1,362,193)	(1,130,655)	(231,538)
Transfers	0	2,349,139	(2,349,139)
Assets January 1, 2002	\$291,015,290	\$247,794,953	\$43,220,337

**BLUE CROSS BLUE SHIELD OF FLORIDA  
STATEMENT OF MEDICARE PENSION ASSETS FOR  
1994 TO 2003**

Description	Total Company	Other Segment	Medicare
Assets January 1, 2002	\$291,015,290	\$247,794,953	\$43,220,337
Prepayment Transfer	0	(2,845,810)	2,845,810
Contribution	86,394,313	86,184,667	209,646
Earnings	(22,741,013)	(19,122,421)	(3,618,592)
Benefit Payments	(11,999,282)	(10,571,420)	(1,427,862)
Expenses	(1,286,037)	(1,081,400)	(204,637)
Transfers	0	2,278,291	(2,278,291)
Assets January 1, 2003	\$341,383,271	\$302,636,860	\$38,746,411
Per Florida	<u>8/</u> \$341,383,271	\$303,931,466	\$37,451,805
Asset Variance	<u>9/</u> \$0	(\$1,294,606)	\$1,294,606

**FOOTNOTES**

- 1/ We determined the Medicare segment assets as of January 1, 1994, in our prior review of Florida's pension segmentation (A-07-94-01107). The amounts shown for the other segment represent the difference between the total company and the Medicare segment. All pension assets are shown at market value.
- 2/ We obtained total company contribution amounts from the actuarial valuation reports. We allocated total company contributions to the Medicare segment based on the ratio of the Medicare segment funding target divided by the total company funding target. Contributions in excess of the funding targets were treated as prepayment credits and accounted for in the "other" segment until needed to fund pension cost in the future.
- 3/ We obtained investment earnings from actuarial valuation reports. Florida allocated its investment earnings based on a ratio of beginning-of-year segment assets to total company assets. We allocated investment earnings for years prior to 1996 using Florida's methodology. For years starting with 1996, we allocated investment earnings based on the ratio of the segment's WAV of assets to total company WAV of assets as required by CAS.
- 4/ We based the Medicare segment's benefit payments on actual payments to Medicare retirees. Florida provided us with supporting documentation for benefit payment amounts to plan retirees. We used actual benefit payments for Medicare segment retirees.
- 5/ We allocated administrative expenses to the Medicare segment in proportion to investment income. Florida used the same methodology.

**BLUE CROSS BLUE SHIELD OF FLORIDA  
STATEMENT OF MEDICARE PENSION ASSETS FOR  
1994 TO 2003**

- 6/ We identified participant transfers between segments by comparing valuation data files provided by Florida. Our transfer adjustment considered each participant's actuarial liability and the funding level of the segment from which the participant transferred. For transfers occurring prior to the 1996 plan year, asset transfers reflected the funding level of the segment from which the participant transferred, based on the actuarial liability and the asset value used for cost purposes. We calculated the funding level as the assets divided by the liabilities. If the funding level was greater than one, we transferred assets equal to the participant's liability. For plan years starting with 1996, asset transfers were equal to the actuarial liability determined under the accrued benefit cost method in accordance with CAS.
- 7/ Prepayment credits represent funds available to satisfy future funding requirements and are applied to future funding requirements before current year contributions in order to reduce interest costs to the Government. Prepayment credits are transferred to the Medicare segment as needed to cover funding requirements.
- 8/ We obtained total asset amounts as of January 1, 2003, from Florida's actuarial valuation report.
- 9/ The asset variance represents the difference between the OIG calculation of Medicare segment assets and Florida's market value of assets shown in its valuation report.



A CMS CONTRACTED INTERMEDIARY & CARRIER

**MEDICARE**

Sandy Coston  
President/COO  
First Coast Service Options  
Sandy.Coston@fcsso.com

January 7, 2005

Mr. James P. Aasmundstad  
Regional Inspector General for Audit Services  
Department of Health and Human Services  
Office of Inspector General  
Office of Audit Services  
601 East 12th Street, Room 284A  
Kansas City, Missouri 64106

Dear Mr. Aasmundstad:

**Reference: A-07-04-00172**

The purpose of this letter is to submit our response to the Department of Health and Human Services Office of Inspector General's draft report for the review of Blue Cross Blue Shield of Florida's (BCBSF) segmentation of Medicare pension assets for fiscal years 1994-2003.

We agree with the report finding regarding the understatement of Medicare segment assets and will take the following action to ensure the report recommendation is implemented.

- 1) Make adjustments to increase the Medicare segment pension assets by \$1,294,606 and recognize segment assets of \$38,746,411 as of January 1, 2003.

Additionally, we are working with BCBSF's actuaries to ensure that Medicare segment assets are updated in accordance with Medicare contractual requirements. We will begin using the weighted average value (WAV) of assets to determine the investment income and expenses allocated to the Medicare segment pension assets, as opposed to the previous methodology that based such allocations on the beginning of year assets.

We appreciate the opportunity to review and provide our comments prior to release of the final report. If you have any questions regarding our response, please contact Mr. Gregory England at 904-791-8364.

Sincerely,

Sandy Coston

cc: Mike Davis, VP & CFO, FCSO  
Gregory England, Director of Internal Audit, FCSO  
Brenda Francisco, Director of Medicare Reporting, FCSO  
Curtis Lord, CEO, FCSO  
Cheryl Mose, Enterprise Controller, BCBSF  
Jay Pinkerton, Chicago Consulting Actuaries, LLP